

**ST 99-8**

**Tax Type: SALES TAX**

**Issue: Bearing the Burden for Payment of Tax (Claim Issues)**

**STATE OF ILLINOIS  
DEPARTMENT OF REVENUE  
OFFICE OF ADMINISTRATIVE HEARINGS  
CHICAGO, ILLINOIS**

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**THE DEPARTMENT OF REVENUE  
OF THE STATE OF ILLINOIS**

**v.**

**“BUILD ‘EM UP SUPPLY CO, INC”,  
Taxpayer**

**No. 97-ST-0000  
IBT No. 0000-0000  
Claim for Credit or Refund**

**Charles E. McClellan  
Administrative Law Judge**

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**RECOMMENDATION FOR DECISION**

**Appearances:**

Mr. Charles Hickman, Special Assistant Attorney General, for the Illinois Department of Revenue; Gregory A. Mescher and James Konsky of Vonachen, Lawless, Trager & Slevin, for the taxpayer.

**Synopsis:**

This matter involves a tentative denial of a claim for credit or refund of Retailers' Occupation Tax paid for the period beginning July 1, 1992, and ending on December 31, 1995, in the amount of \$149,214. The claim asked for a refund of taxes paid, pursuant to an audit, on materials sold by the taxpayer in connection with construction projects in two enterprise zones. The parties entered into a stipulation of facts regarding the documentation of the transactions involved in this matter. In addition to the stipulation, an evidentiary hearing was held at the Department's office in "Nowhere", Illinois<sup>1</sup>. Both parties filed briefs. My recommendation is that the tentative denial be cancelled and the refund claim be allowed.

**Finding of Fact:**

1. “Build ‘Em Up Supply Co., Inc. (“taxpayer”) was incorporated in 1989 and was in good standing from July 1, 1992 through December 31, 1995. Tr. p. 107; Stip. ¶ 1.

2. Taxpayer is a wholly owned subsidiary of “Tear ‘Em Down Construction Co.”, that was formed for the purpose of taking advantage of the enterprise zone exemption. *Id.*

3. Taxpayer maintains separate books and records and is included in the consolidated income tax return of “Tear ‘Em Down Construction Co.” *Id.*

4. During the tax periods, taxpayer rented its own post office box. Tr. p. 72.

5. During the periods at issue, “Tear ‘Em Down Construction Co.” was the general contractor on a construction project in the enterprise zone established by the city of “Toon Town”, Illinois for the CEFCU project. Tr. p. 108.

6. Taxpayer entered into an oral agreement with “Stick Tight Painting”, a subcontractor, for the use of the back office in its building (the “Stick Tight” building) located at 4000 W. Memory Lane in “Toon Town”, Illinois. Tr. pp. 40, 110, 111.

7. Taxpayer maintained its vendor files for the CEFCU project, consisting of purchase orders, invoices and other documents related to its vendors, in a file cabinet in the office it maintained in the “Stick Tight” building. Tr. p. 111.

8. As the general contractor, “Tear ‘Em Down Construction Co. sub-contracts about 75% to 80% of the work. Tr. p 112.

9. For a project such as CEFCU there would be 20 to 25 subcontractors and one purchase order received from each subcontractor. Tr. p. 113.

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<sup>1</sup> The evidentiary hearing was conducted by an administrative law judge who is now on leave of absence from the Department. There is no issue as to the credibility of witnesses.

10. For a project such as CEFCU, “Tear ‘Em Down Construction Co. would issue five or six purchase orders and the taxpayer would process about forty purchase orders from the beginning to the end of the project. Tr. p. 114.

11. As the CEFCU project proceeded, taxpayer would receive invoices from vendors for which it would then invoice the subcontractors and the contractor. *Id.*

12. The volume of purchase orders for a project such as CEFCU could be processed in about one-half day but the processing actually occurs over a three or four month period as the project is starting up. Tr. p. 116.

13. The equipment required to process these documents were a desk a chair, a file cabinet, and a laptop computer to maintain the vendor files. Tr. pp. 70, 117.

14. No rent was paid to “Stick Tight” for the use of the “Toon Town” office and no telephone was required. Tr. p. 119.

15. During the tax period, “Tear ‘Em Down Construction Co. also did a project for the “Harold Hill” Athletic Club and an office remodeling project for “Butterfly”, Inc., in the “Nowhere” enterprise zone. Tr. p. 109, 120.

16. During the periods at issue, “Tear ‘Em Down Construction Co.” was also the general contractor for the “Toon Town” office and parking deck in an enterprise zone in “Nowhere”, Illinois. Tr. p. 109.

17. On January 1, 19xx, taxpayer signed a lease to rent office suite number 103 at 7000 N. “Carriage” Avenue, “Nowhere”, Illinois (“Nowhere suite”) . Tr. pp. 54, 55, 121, Taxpayer Ex. No. 1.

18. The building located at 7000 N. “Carriage” Avenue is owned, in part, by “Matty Hayes” whose husband is a majority stockholder in “Tear ‘Em Down Construction Co.”, which constructed the building. Tr. p. 122.

19. Taxpayer never paid rent for the “Nowhere” suite because the owners waived it. Tr. p. 123.

20. The office was equipped with filing cabinets a calculator and a desk. Tr. p. 56.

21. Taxpayer had keys for the “Nowhere” suite, which had a separate entrance. Tr. pp. 57, 64

22. Taxpayer had no assets or employees. Tr. p. 16.

23. Taxpayer’s purchase orders, invoices, and check writing functions were performed from time to time on an as-needed basis by various employees of “Tear ‘Em Down Construction Co.” in its “Toon Town” location for the “Toon Town” enterprise zone project and in “Nowhere” for the “Nowhere” enterprise zone projects. Tr. pp. 67, 88, 92, 116, 125.

24. Taxpayer did not maintain regular business hours either at its “Toon Town” office or at its “Nowhere” office because it was not necessary. Tr. p. 126

25. All transactions covered by the audit report and which are the subject of this hearing were retail sales of building materials to be incorporated into real estate (by remodeling, rehabilitation or new construction) located in the enterprise zones of “Toon Town” Illinois and “Nowhere” Illinois. Stip. ¶¶ 2, 5.

26. With respect to the transactions covered by the audit report and which are the subject of the administrative hearing, the books and records of taxpayer contain written statements signed by the purchasers setting forth the following information:

- (a) A certification by the purchaser that the building materials being purchased are being purchased for incorporation into real estate located in an enterprise zone;

- (b) A description of the building materials being purchased;
- (c) The location of the real estate into which building materials will be incorporated;
- (d) The name of the enterprise zone in which that real estate is located;
- (e) The purchaser's signature and date of signing. Stip. ¶ 3.

27. Taxpayer was registered with the Illinois Department of Revenue as a retailer with locations in "Nowhere", Illinois, "Toon Town", Illinois, and East "Nowhere" Illinois, during all periods relevant from July 1, 1992 through December 31, 1995. Stip. ¶ 4.

28. The books and records of taxpayer contain the following documentation for each sale from the supplier to taxpayer with regard to each transaction covered by the audit report and which are the subject of this hearing:

- a. Purchase order from taxpayer to the supplier;
- b. Certificate of resale from taxpayer to the supplier;
- c. Invoice from the supplier to taxpayer;
- d. Payment to the supplier from taxpayer. Stip. ¶ 6.

29. The books and records of taxpayer contain the following documentation for each sale from taxpayer to the purchaser with regard to each transaction covered by the audit report and which are the subject of the administrative hearing:

- a. Written purchase order from the purchaser to taxpayer, except for the few occasions when a purchaser may have orally ordered building materials from taxpayer;
- b. An enterprise zone building materials certification from the purchaser to taxpayer containing all of the information set forth in

Section 130.1951(a)(6) of the Illinois Administrative Code, as amended January 27, 1998;

- c. Invoice from taxpayer to the purchaser;
- d. Payment to taxpayer from the purchaser.

### **Conclusions of Law**

The Illinois Enterprise Zone Act was enacted by P. A. 82-1019, effective December 7, 1982, “to explore ways and means of stimulating business and industrial growth and retention in depressed areas and stimulating neighborhood revitalization of depressed areas of the State by means of relaxed government controls and tax incentives in those areas.” 20 ILCS 655/2. P. A. 82-1019 also amended the Retailers’ Occupation Tax by adding section 5k which, for the years at issue, provided in relevant part:

Each retailer whose place of business is within a county or municipality which has established an Enterprise zone pursuant to the Illinois Enterprise Zone Act and who makes a sale of building materials to be incorporated into real estate in such enterprise zone by remodeling, rehabilitation or new construction, may deduct receipts from such sales when calculating the tax imposed by this Act. 35 ILCS 120/5k.

The regulations issued by the Department, as they were in effect for the tax periods, set forth detailed record keeping requirements for retailers located in municipalities or counties that have established enterprise zones and who are selling building materials for incorporation into real estate being rehabilitated, remodeled or constructed in those zones. 86 Admin. Code ch. I, § 130.1951. The parties’ have stipulated that the taxpayer’s records satisfy those requirements.

However, the Department asserts that taxpayer did not establish bona fide retail establishments in the “Toon Town” and “Nowhere” enterprise zones because it was not staffed on a regular basis, had no telephone, paid no rent or utilities for the space and failed to conduct regular business operations at that location. The auditor had no knowledge of

taxpayer's operation in the "Toon Town" enterprise zone, but the Department is arguing the same theory with respect to it.

The taxpayer counters that it was not necessary to maintain normal business hours at its locations in "Toon Town" and "Nowhere" and that it fulfilled all of the statutory and regulatory requirements necessary to claim the enterprise zone exemption as they were in effect for the years at issue.

Neither the statute nor the regulations applicable to the tax periods address the question of what constitutes having a "place of business" within a municipality or an unincorporated area of a county which has established an enterprise zone. There is no definition of "retailer" nor are there any provisions that prescribe how much substance needs to be put in a corporation established by a contractor to act as a retailer in a municipality or an unincorporated area of a county which has established an enterprise zone.

Taxpayer registered its locations in "Toon Town" and in "Nowhere" with the Department. It would be unreasonable to expect taxpayer to maintain normal business hours staffed with personnel at the "Toon Town" and "Nowhere" locations if there was no need for them. Such a requirement would be a waste of time and money. Taxpayer called five witnesses at the hearing all of which testified that the purchase orders, invoices and checks for the enterprise zone projects were processed in "Toon Town" and "Nowhere" in each case. Their testimony was not controverted. The Department points out in its brief that taxpayer's witnesses testified that some enterprise zone paper work may have been processed in the East "Nowhere" offices of taxpayer's parent corporation, "Tear 'Em Down Construction Co." However, there is no testimony or other evidence indicating that such paper work involved sales that are the subject of the claim in this case.

The Department states that “the taxpayer did not introduce any evidence as to any particular transaction as to where the documentation for that transaction might have been processed.” The Department then argues that there must be a determination that all transactions qualify for the enterprise zone exemption. No authority is cited for this proposition. In addition, this argument fails to take into account that the parties stipulated that the documentation regarding the transactions involved in this case satisfied the record keeping requirements of the regulations as they existed for the tax periods at issue.

The Department next states, incorrectly, that regulation 130.1951(a)(2) (86 Admin. Code ch. I, § 130.1951(a)(2)), as it applied during the tax periods, required that “the retailer must be located in the enterprise zone for sales of building materials to qualify for the enterprise zone exemption.” That regulation did not then, and does not now, contain any such requirement. It simply follows the statute in requiring that the retailer maintain a place of business in the municipality or in the unincorporated area of the county that has established the enterprise zone. Taxpayer in this case complied with that requirement.

Finally, the Department argues that taxpayer was obligated to document that the purchase orders in question were accepted in the enterprise zone. During the tax periods at issue, there was no such requirement in the regulations. Effective January 27, 1998, long after the tax periods at issue, the regulation was amended to add a requirement that the retailer “be able to document the acceptance of the purchase orders at a location in the municipality or the unincorporated area of the county that has established the enterprise zone.” 22 Ill. Reg. 3097.

This argument is an attempt by the Department to apply the amended regulation retroactively. The Illinois Supreme Court has held that it is unreasonable and inequitable to apply a regulation retroactively where taxpayers have entered into contracts on the basis

of existing regulations. Pressed Steel Car Company v. Lyons, 7 Ill. 2d 95 (1955). Once an administrative agency has adopted a regulation implementing a statute, it must adhere to it as long as it is in effect. Illinois Bell Telephone Company v. Allphin, 95 Ill. App. 3d 115 (1st Dist. 1981). In order to prevail with this argument, the 1998 amendment to the regulation would have to be applied to transactions that occurred over three years prior to the effective date of amendment. That would be grossly unfair to the taxpayer that relied on the regulations as they existed at the time it entered into its contracts for the enterprise zone projects, and it would be contrary to the precedents cited above.

There is nothing in the statute that prevents a taxpayer from arranging its affairs to minimize taxes. See First Chicago Building Corp. v. Department of Revenue, 49 Ill. App. 3d 237 (1st Dist. 1977). That is what the taxpayer and its parent corporation did in this case. Taxpayer's creation and function were consistent with the legislative intent in enacting the Illinois Enterprise Zone Act. See Craftmasters v. Department of Revenue, 269 Ill. App. 3d 934 (4th Dist. 1994) For all of the reasons stated above, I conclude that the testimony and evidence of record submitted by the taxpayer is sufficient to overcome the Department's *prima facie* case.

THEREFORE, I recommend that the taxpayer's claim be allowed.

**Date: 3/31/99**

**ENTER:**

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**Administrative Law Judge**